

# EXHIBIT 8

**THE METROPOLITAN SEWER DISTRICT  
OF GREATER CINCINNATI**

***FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT***

**December 31, 1996**

**THE METROPOLITAN SEWER DISTRICT  
OF GREATER CINCINNATI**

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**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
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Certified Public Accountants and Business Advisors

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Fort Mitchell, Kentucky 41017-5610

4221 Malsbary Road Suite 102  
Cincinnati, Ohio 45242-5502

**INDEPENDENT AUDITORS' REPORT**

The Honorable Board of County Commissioners  
The Metropolitan Sewer District of Greater Cincinnati  
County of Hamilton, Ohio

We have audited the balance sheets of The Metropolitan Sewer District of Greater Cincinnati (MSD), a component unit of the County of Hamilton, Ohio, as of December 31, 1996 and 1995, and the related statements of revenues, expenses and changes in fund equity, and cash flows for the years then ended. These financial statements are the responsibility of MSD's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Metropolitan Sewer District of Greater Cincinnati, at December 31, 1996 and 1995, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 25, 1997 on our consideration of The Metropolitan Sewer District of Greater Cincinnati's internal control structure and a report dated April 25, 1997 on its compliance with laws and regulations.

*VonLehman & Company Inc.*

Fort Mitchell, Kentucky  
April 25, 1997

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**BALANCE SHEETS**  
 December 31, 1996 and 1995  
 (amounts expressed in thousands)

**ASSETS**

	1996	1995
<b>Current Assets</b>		
Cash and Cash Equivalents	\$ 11,786	\$ 11,805
Accounts Receivable	19,035	16,450
Prepaid Expenses and Other	3,307	1,896
<b>Total Current Assets</b>	<u>34,128</u>	<u>30,151</u>
<b>Restricted Assets</b>		
Cash and Cash Equivalents Held by the City of Cincinnati		
Construction Account	5,246	9,694
Amount to be Transferred to Surplus Account	10,988	10,639
Investments Held by Trustee		
Cash and Cash Equivalents	846	2,456
Investments - Held to Maturity	66,583	89,199
<b>Total Restricted Assets</b>	<u>83,663</u>	<u>111,988</u>
<b>Property, Plant and Equipment</b>		
Land	4,282	3,962
Buildings and Structures	468,292	415,903
Processing Systems	216,726	206,341
Office and Service Equipment	20,934	18,444
Construction in Progress	97,669	110,272
	807,903	754,922
Accumulated Depreciation	<u>(254,168)</u>	<u>(233,989)</u>
<b>Total Property, Plant and Equipment</b>	<u>553,735</u>	<u>520,933</u>
<b>Other Assets</b>		
Unamortized Financing Costs	8,241	8,838
Settlements Receivable	917	917
Other	3,101	3,109
<b>Total Other Assets</b>	<u>12,259</u>	<u>12,864</u>
<b>Total Assets</b>	\$ <u>683,785</u>	\$ <u>675,936</u>

**LIABILITIES AND EQUITY**

	1996	1995
<b>Current Liabilities</b>		
Current Portion of Long-Term Debt	\$ 9,250	\$ 8,906
Accounts Payable	3,576	2,833
Accrued Payroll Expenses	1,271	1,054
<b>Total Current Liabilities</b>	<u>14,097</u>	<u>12,793</u>
<b>Payable from Restricted Assets</b>		
Construction Accounts Payable	3,866	5,068
Accrued Interest	1,308	1,341
<b>Total Payable from Restricted Assets</b>	<u>5,174</u>	<u>6,409</u>
<b>Long-Term Liabilities</b>		
Accrued Compensated Absences	5,476	5,300
Long-Term Debt (Net of Deferred Loss on Refunding Bonds of \$574 in 1996 and \$1,034 in 1995)	295,581	300,796
<b>Total Long-Term Liabilities</b>	<u>301,057</u>	<u>306,096</u>
<b>Total Liabilities</b>	<u>320,328</u>	<u>325,298</u>
<b>Equity</b>		
Contributions in Aid of Construction	173,173	174,634
Retained Earnings	190,284	176,004
<b>Total Equity</b>	<u>363,457</u>	<u>350,638</u>
<b>Total Liabilities and Equity</b>	\$ <u>683,785</u>	\$ <u>675,936</u>

See auditors' report and accompanying notes.

**LIABILITIES AND EQUITY**

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STATE OF OHIO  
OFFICE OF THE AUDITOR

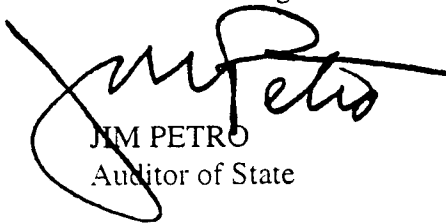
JIM PETRO, AUDITOR OF STATE

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Board of County Commissioners  
Metropolitan Sewer District of Greater Cincinnati

We have reviewed the independent auditor's report of the Metropolitan Sewer District of Greater Cincinnati, Hamilton County, prepared by VonLehman & Company Inc. for the audit period January 1, 1996 through December 31, 1996. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Metropolitan Sewer District of Greater Cincinnati is responsible for compliance with these laws and regulations.



JIM PETRO  
Auditor of State

December 12, 1997



STATE OF OHIO  
OFFICE OF THE AUDITOR

JIM PETRO, AUDITOR OF STATE

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Enclosed is your public office's audit report. The unbound copy is for your use in making appropriate copies for each of your grantors, as required by the Single Audit Act of 1984. This office will forward one (1) copy of your audit to the National Single Audit Clearinghouse in Indiana. Generally, you must transmit the copies to your grantor within 30 days of your receipt of the audit report from us.

If you have any questions, please contact your local district audit office.

Sincerely,

JIM PETRO  
Auditor of State

A handwritten signature in cursive script, reading "Jill M. Burch".

Jill M. Burch  
Clerk of the Bureau

JMB/vjb

Enclosure

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
**STATEMENTS OF REVENUES, EXPENSES  
AND CHANGES IN FUND EQUITY**  
Years Ended December 31, 1996 and 1995  
(amounts expressed in thousands)

	<u>1996</u>	<u>1995</u>
<b>Operating Revenues</b>		
Sewerage Service Charges	\$ 90,189	\$ 84,258
Sewerage Surcharges	11,525	11,439
Other Revenues	<u>2,749</u>	<u>3,459</u>
Total Operating Revenues	<u>104,463</u>	<u>99,156</u>
<b>Operating Expenses</b>		
Personnel Services	35,779	34,431
Utilities, Fuel and Supplies	14,183	13,003
Depreciation and Amortization	21,743	21,201
Purchased Services	13,965	14,264
Other Expenses	<u>3,133</u>	<u>4,211</u>
Total Operating Expenses	<u>88,803</u>	<u>87,110</u>
<b>Income from Operations</b>	<u>15,660</u>	<u>12,046</u>
<b>Other Income (Expense)</b>		
Interest Income	5,792	5,031
Gain on Disposal of Property, Plant and Equipment	390	31
Gain on Redemption of Investments	-	1,844
Interest Expense	<u>(15,262)</u>	<u>(12,818)</u>
Total Other Income (Expense)	<u>(9,080)</u>	<u>(5,912)</u>
<b>Net Income</b>	6,580	6,134
Amortization of Contributions in Aid of Construction	7,700	7,706
Retained Earnings at Beginning of Year	<u>176,004</u>	<u>162,164</u>
<b>Retained Earnings at End of Year</b>	<u>190,284</u>	<u>176,004</u>
Contributions in Aid of Construction at Beginning of Year	174,634	178,114
Additions to Contributions in Aid of Construction	6,239	4,226
Amortization of Contributions in Aid of Construction	<u>(7,700)</u>	<u>(7,706)</u>
<b>Contributions in Aid of Construction at End of Year</b>	<u>173,173</u>	<u>174,634</u>
<b>Total Fund Equity at End of Year</b>	<u>\$ 363,457</u>	<u>\$ 350,638</u>

See auditors' report and accompanying notes.

## THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI

## STATEMENTS OF CASH FLOWS

Years Ended December 31, 1996 and 1995

(amounts expressed in thousands)

	1996	1995
<b>Cash Flows from Operating Activities</b>		
Cash Received from Customers	\$ 99,569	\$ 95,559
Cash Payments for Goods and Services	(31,996)	(31,497)
Cash Payments for Personnel Costs	(35,385)	(34,683)
Other Operating Revenues	2,309	3,584
<b>Net Cash Provided by Operating Activities</b>	<u>34,497</u>	<u>32,963</u>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Proceeds from Sale of Revenue Bonds	-	65,171
Principal and Interest Payments on Long-Term Debt	(21,938)	(21,647)
Acquisition and Construction of Capital Assets	(51,062)	(48,341)
Grants and Contributions	2,965	904
Proceeds from Sale of Property, Plant and Equipment	390	41
<b>Net Cash Used for Capital and Related Financing Activities</b>	<u>(69,645)</u>	<u>(3,872)</u>
<b>Cash Flows from Investing Activities</b>		
Purchase of Government Securities	(162,944)	(175,556)
Maturity or Redemption of Government Securities	185,426	139,382
Interest Earned on Investments	6,997	6,200
Trustee Fees	(59)	(98)
<b>Net Cash Provided (Used) by Investing Activities</b>	<u>29,420</u>	<u>(30,072)</u>
Net Change in Cash and Cash Equivalents	(5,728)	(981)
Cash and Cash Equivalents at January 1	<u>34,594</u>	<u>35,575</u>
<b>Cash and Cash Equivalents at December 31</b>	<u>\$ 28,866</u>	<u>\$ 34,594</u>
<b>Reconciliation of Operating Income to Net Cash Provided by Operating Activities:</b>		
Income from Operations	\$ 15,660	\$ 12,046
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	21,743	21,201
Allowance for Doubtful Accounts	300	200
Change in Assets and Liabilities:		
Net Change in Customer Accounts Receivable	(2,445)	(338)
Net Change in Other Receivable	(440)	125
Net Change in Prepaid Expenses	(1,412)	(22)
Net Change in Operating Accounts Payable	393	3
Net Change in Accrued Payroll and Related Expenses	698	(252)
<b>Net Cash Provided by Operating Activities</b>	<u>\$ 34,497</u>	<u>\$ 32,963</u>
<b>Noncash Investing and Financing Transactions</b>		
Equipment Received in as Partial Payment for Settlement Receivable	\$ -	\$ 400
Loans Incurred for Construction	3,579	3,824
Structures Acquired as Contributed Capital in Aid of Construction	3,999	4,226
Expenses Related to Bonds Issued	-	1,421
Escrowed Amounts for Defeased Bonds	-	19,208
<b>Total Noncash Investing and Financing Transactions</b>	<u>\$ 7,578</u>	<u>\$ 29,079</u>

See auditors' report and accompanying notes.

## **NOTE 1 - ACCOUNTING POLICIES**

A summary of the significant accounting policies applied in the accompanying financial statements follows:

### **Organization**

The Metropolitan Sewer District of Greater Cincinnati (MSD) collects and treats industrial and residential wastewater for municipalities and unincorporated areas of Hamilton County. MSD was established pursuant to an agreement dated May 1, 1968 between the Board of Commissioners of Hamilton County and the City of Cincinnati. Under a contract with the City of Cincinnati, the Board designated the City as its agent for the maintenance and operation of MSD. The annual budget, prepared on the cash basis of accounting, is approved by the Board and administered by the City. Budgetary control is exercised at the divisional level, and between personnel and all other costs.

### **Basis of Accounting**

The accompanying financial statements were prepared on the accrual basis of accounting, whereby revenues and expenses are recognized in the period earned or incurred.

### **Proprietary Activity Accounting and Financial Reporting**

Under the Governmental Accounting Standards Board Statement (GASB) No. 20, Accounting and Financial Reporting for Proprietary Activities, the District has elected the option to apply all Financial Standards Board Statements (FASB) and Interpretations issued on or before November 30, 1989, except those that conflict with or contradict GASB pronouncements.

### **Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### **Investments**

MSD is required by Ohio law to invest in only United States obligations; federal agency securities; Ohio bonds and other obligations or such obligations of political subdivisions of the state, provided that the subdivisions are located within Hamilton County; time certificates of deposit or deposit accounts in an eligible institution; and no load money market mutual funds consisting only of investments mentioned above. Investments are required to mature within five years from the date of settlement, unless the investment is matched to a specific obligation or debt of MSD. MSD has the ability and intent to hold all investments to maturity and under the provisions of FAS 115 have classified all investments as "held to maturity".

Investment securities are stated at cost, adjusted for amortization of premiums and accretion of discounts on purchases. Amortization and accretion is by the straight-line method over the term of the investment. Any differences between amortization or accretion by the straight-line method versus the interest method are immaterial.

**NOTE 1 - ACCOUNTING POLICIES (Continued)**

**Inventory**

Supplies and materials are stated at the lower of cost or market on a first-in, first-out (FIFO) basis.

**Property, Plant and Equipment**

Property, plant and equipment are stated at historical cost for assets acquired after MSD's inception in 1968. Assets which were acquired prior to 1968 and not identifiable with specific historical costs are not included in the property, plant and equipment balance. Assets acquired by MSD through contributions, such as contributions from land developers and federal and state grants, are capitalized and recorded in the plant records at the contributors' reported cost. Construction costs include interest capitalized on debt during the period of construction and the cost of in-force labor.

Depreciation expense is computed on the straight-line method over the estimated useful lives of the respective assets. The estimated lives are as follows:

Building and Structures	40 Years
Processing Systems	25 Years
Office and Service Equipment	5 - 15 Years

Depreciation expense on fixed assets acquired through contributions is reported as an offset against contributions in aid of construction in fund equity. Any gain or loss arising from the disposal of fixed assets has been credited or charged to income.

**Unamortized Financing Costs**

The unamortized financing costs include bond discount, consulting and attorney fees incurred in connection with the revenue bond obligations. These amounts are being amortized on the interest method and the straight-line method, respectively, over the lives of the revenue bonds.

**Pension Plans**

Employees participate in either the City of Cincinnati's Retirement System or the Public Employees Retirement System administered by the State of Ohio. Pension costs reflect a percentage of employees' gross pay, as defined by the terms of pension plans in which employees participate. MSD's policy is to fund pension costs accrued.

**Insurance**

MSD participates in Ohio Workers' Compensation and Ohio State Unemployment programs through the City of Cincinnati.

**NOTE 1 - ACCOUNTING POLICIES (Continued)**

**Compensated Absences**

Compensated absences are accrued in accordance with Statement No. 16 issued by the Governmental Accounting Standards Board. Components of the liability include accrued vacation time, sick leave, compensatory time and other related payments.

**NOTE 2 - CASH AND CASH FLOW INFORMATION**

For purposes of the Statement of Cash Flows, all highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents.

**NOTE 3 - CASH AND INVESTMENTS**

Cash and investments consist of the following at December 31, 1996 and 1995:

(in thousands)	1996		1995	
	Cash and Cash Equivalents	Investments	Cash and Cash Equivalents	Investments
Amounts held by City of Cincinnati	\$28,020	\$ -	\$32,138	\$ -
Investments held by Trustees:				
Reserve	841	27,652	103	26,617
Replacement and Improvement	1	4,948	-	5,063
Expense Fund	-	-	74	-
Bond Retirement	2	2,213	2,279	-
Surplus	<u>2</u>	<u>31,770</u>	<u>-</u>	<u>57,519</u>
Total cash and investments	<u>\$28,866</u>	<u>\$66,583</u>	<u>\$34,594</u>	<u>\$89,199</u>

The amounts held by the City of Cincinnati (the City) are invested on MSD's behalf in accordance with the Cincinnati Municipal Code. These amounts are collateralized as part of the City's cash and investment balances. Bank balances of the City are covered by Federal depository insurance or collateral held by the Cincinnati Branch of the Federal Reserve Bank of Cleveland or the City's agent in the City's name.

Investments held by trustees are eligible investments as defined by the Trust Agreement and are registered in the name of the trustee for the benefit of MSD.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 1996 and 1995**

**NOTE 3 - CASH AND INVESTMENTS (Continued)**

Insured investment securities held to maturity at December 31, 1996 and 1995 consist of the following:

(in thousands)	<u>Carrying Value</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Estimated Market Value</u>
<u>December 31, 1996</u>				
U.S. Government Treasury Bills	\$39,007	\$452	\$ -	\$39,459
U.S. Government Treasury Notes	11,577	-	359	11,218
U.S. Government Treasury Bonds	<u>15,999</u>	<u>-</u>	<u>664</u>	<u>15,335</u>
Totals	<u>\$66,583</u>	<u>\$452</u>	<u>\$1,023</u>	<u>\$66,012</u>
 <u>December 31, 1995</u>				
U.S. Government Treasury Bills	\$62,458	\$ 462	\$ -	\$63,043
U.S. Government Treasury Notes	10,625	231	-	10,856
U.S. Government Treasury Bonds	<u>15,993</u>	<u>608</u>	<u>-</u>	<u>16,601</u>
Totals	<u>\$89,199</u>	<u>\$ 1,301</u>	<u>\$ -</u>	<u>\$90,500</u>

**NOTE 4 - ACCOUNTS RECEIVABLE**

Accounts receivable as of December 31, 1996 and 1995, consisted of the following:

	(in thousands)	
	<u>1996</u>	<u>1995</u>
Sewerage charges and surcharges:		
Unbilled amount	\$ 9,639	\$ 8,643
Billed amount	9,679	8,230
Less allowable for doubtful accounts	(1,220)	(920)
Other	<u>2,507</u>	<u>497</u>
Total	<u>\$20,605</u>	<u>\$16,450</u>

**NOTE 5 - RESTRICTIONS ON ASSETS**

Land acquired for MSD's use is titled to either the City of Cincinnati or Hamilton County. The cost of this land has been recorded on the books of MSD since it has the full benefits of the land as an economical resource.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 1996 and 1995**

**NOTE 5 - RESTRICTIONS ON ASSETS (Continued)**

In August 1985, the Federal District Court entered a consent order in an action with MSD and others (see Commitments and Contingencies Note). In complying with the consent order, MSD is required to maintain amounts on deposit in an environmental security account. Expenditures from this account must be approved by the U.S. Environmental Protection Agency. The balance of this account, which is included in other assets, was \$902,000 and \$859,000 at December 31, 1996 and 1995, respectively.

The Trust Agreement for the Series A Revenue Bonds (see Long-Term Debt Note) requires the establishment of certain trust accounts including a Bond Account, Bond Reserve Account, Replacement and Improvement Account, and a Surplus Account to be held by the Trustee. The Bond Account will be used to accumulate periodic principal and interest payments. The Bond Reserve Account will be funded in an amount equal to the highest annual future debt service requirement. The Replacement and Improvement Account will be maintained with a balance of \$5,000,000. The Surplus Account is available to be used for any other Sewer System purpose. The Trust Agreement also requires the creation of a Construction Account to be held by the City to pay for project costs.

**NOTE 6 - LONG-TERM DEBT**

As of December 31, 1996 and 1995, long-term debt consisted of the following:

(in thousands, except percents)

	Principal Issue	Interest Rate	Year of Maturity	1996	1995
Series A Revenue Bonds					
1995	\$ 85,800	3.70-6.05	2017	\$ 84,130	\$ 85,535
1993	171,790	2.45-5.60	2016	166,230	167,015
1991	90,950	4.80-6.70	2013	37,840	41,950
1986	85,020	4.90-7.50	2011	-	940
Loveland Sewer District	200	5.75	2000	40	50
Ohio Water Development Authority Contracts	41,830	2.00-7.49	2019	7,080	8,341
Ohio Water and Sewer Rotary Commission	-	-	-	124	124
Ohio Public Works Commission	-	0.00-3.00	2017	2,203	1,366
Water Pollution Control Loan Fund - Construction	-	3.54-4.80	2018	7,686	5,291
Drawdown	-	7.35	1998	72	124
Capital Lease	293				
Total Obligations				305,405	310,736
Less Current Maturities				9,250	8,906
Long-Term Portion				296,155	301,830
Less Deferred Loss on Refunding				574	1,034
Long-Term Portion				<u>\$295,581</u>	<u>\$300,796</u>

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
NOTES TO THE FINANCIAL STATEMENTS  
December 31, 1996 and 1995

**NOTE 6 - LONG-TERM DEBT (Continued)**

Principal payments on long-term debt for the next five years and thereafter are as follows:

	(in thousands)
1997	\$ 9,250
1998	9,918
1999	10,379
2000	10,875
2001	11,076
Thereafter	<u>253,907</u>
Total	<u>\$305,405</u>

**Series A Revenue Bonds**

Effective August 31, 1995, MSD issued \$85,800,000 County of Hamilton, Ohio 1995 Series A Sewer System Improvement and Refunding Revenue Bonds dated August 15, 1995. The proceeds from the 1995 bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1986 and 1991 Series A bond issues, fund the new bond reserve requirement and pay the cost of issuance. The 1995 bonds are special obligations of the District payable solely from the net revenues of the District and are issued on a parity with the 1985, 1986, 1991 and 1993 Series A bonds, secured equally and ratably under the Trust Agreement.

Effective May 4, 1993, MSD issued \$171,790,000 County of Hamilton, Ohio 1993 Series A Sewer System Improvement and Refunding Revenue Bonds dated April 15, 1993. The proceeds from the 1993 Bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1986 and 1991 Series A bond issues, fund the new bond reserve requirement, and pay the cost of issuance. The 1993 bonds are special obligations of the District payable solely from the net revenues of the District and are issued on a parity with the 1985, 1986 and 1991 Series A bonds, secured equally and ratably under the Trust Agreement.

Effective February 26, 1991, MSD issued \$90,950,000 County of Hamilton, Ohio, 1991 Series A Sewer System Improvement and Refunding Revenue Bonds dated January 15, 1991. The proceeds from the 1991 Bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1985 Series A bond issue, fund the new bond reserve requirement, and pay the cost of issuance.

Effective May 29, 1986 MSD issued \$85,020,000 County of Hamilton, Ohio Sewer System Revenue Bonds, 1986 Series A. The proceeds from the 1986 Bonds were used to fund certain construction projects, establish various trust funds required by the Bond Indenture, and to pay certain fees and expenses incurred with the issuance of the bonds.

**NOTE 6 - LONG-TERM DEBT (Continued)**

The 1995, 1993 and 1991 Bonds may be redeemed prior to their maturities in accordance with provisions of the bond resolutions. The redemption prices for the bonds include declining premiums up to 3 percent of principal.

Maturities for bonds over the next five years and thereafter are shown below.

	(in thousands)		
	1995	1993	1991
	<u>Bonds</u>	<u>Bonds</u>	<u>Bonds</u>
1997	\$ 2,470	\$ 815	\$4,345
1998	2,570	845	4,605
1999	2,685	885	4,875
2000	2,800	930	5,175
2001	5,095	975	3,325
Thereafter	<u>68,510</u>	<u>161,780</u>	<u>15,515</u>
	<u>\$ 84,130</u>	<u>\$166,230</u>	<u>\$37,840</u>

Under the terms of the amended revenue bond trust indenture, MSD has agreed to certain covenants, among other things, to restrict additional borrowing, fix and maintain rates sufficient to meet debt service requirements, and maintain specified fund balances under trust agreements.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 1996 and 1995**

**NOTE 6 - LONG-TERM DEBT (Continued)**

The Revenue Serial bond issues as discussed above contain covenants which require the District to maintain a level of debt service coverage. The following calculation reflects the District's debt service coverage.

	(in thousands)	
	<u>1996</u>	<u>1995</u>
Revenues:		
Total operating revenues	\$104,463	\$ 99,156
Interest Income	5,792	5,031
Capitalized Interest Income	1,072	766
Tap-in / Connection Fees	<u>2,239</u>	<u>-</u>
Total pledge revenues	113,566	104,953
Total operating and maintenance expenses		
less depreciation and amortization	(67,060)	(65,909)
Half of Pledged Revenues Transferred		
to Surplus Account	<u>5,494</u>	<u>5,320</u>
Net income available for debt service	(a)   \$ <u>52,000</u>	\$ <u>44,364</u>
Principal and Interest Requirements on		
Revenue Bonds	(b)   \$ <u>23,328</u>	\$ <u>19,275</u>
Principal and interest requirements on		
all obligations	(c)   \$ <u>25,884</u>	\$ <u>21,479</u>
Debt Service Coverage:		
Revenue Bonds (a) divided (b)	<u>2.23</u>	<u>2.30</u>
All Obligations (a) divided (c)	<u>2.01</u>	<u>2.07</u>
Basic coverage required on bonds	<u>1.25</u>	<u>1.25</u>

**Loveland Sewer District**

Sewer Improvement Bonds in the amount of \$200,000 were issued by the City of Loveland in 1974. MSD assumed this debt upon merger of the Loveland Sewer District into MSD in March, 1985.

**Ohio Water Development Authority Contracts**

All contracts between the Ohio Water Development Authority (OWDA) and the Metropolitan Sewer District require MSD to prescribe and charge such rates for sewer usage which are sufficient (after expenses of operation and maintenance) to pay principal and interest on OWDA contracts. The principal is repayable in equal semi-annual installments to maturity.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 1996 and 1995**

**NOTE 6 - LONG-TERM DEBT (Continued)**

**Tap-in / Connection Fees**

Tap-in / connection fees were increased in 1996. The typical single-family home increased from \$480 to \$2,500. This change meets the criteria for revenue to be recognized as a contribution of capital by the property owner instead of expense recovery as in prior years.

**Ohio Water and Sewer Rotary Commission**

Advances from Ohio Water and Sewer Rotary Commission represent tap-in fees and acreage assessments to be forwarded to the Commission upon collection from customers. Such advances do not bear interest unless they are determined to be in default.

**Ohio Public Works Commission**

The MSD has entered into agreements with the Ohio Public Works Commission (OPWC) for financing of certain qualified capital projects. As the projects progress the commitments are drawn down as funds are paid by OPWC directly to the contractors. The principal is repayable in semi-annual installments to the date of maturity for each project.

**Water Pollution Control Loan Fund**

The MSD has received low interest loan commitments from the Ohio Water Pollution Control Loan Fund for certain qualified projects. As the projects progress the commitments are drawn down.

**Capital Lease**

A five year lease/purchase agreement for communication equipment commenced in 1993 with monthly payments of \$4,661 to 1998.

**Interest on Long-Term Obligations**

For the years 1996 and 1995, the following interest costs were incurred and expensed or capitalized as part of the cost of MSD's additions to property, plant, and equipment.

	(in thousands)	
	<u>1996</u>	<u>1995</u>
Interest Incurred	\$ 17,868	\$ 14,771
Less Interest Capitalization	<u>(2,606)</u>	<u>(1,953)</u>
Interest Expense	\$ <u>15,262</u>	\$ <u>12,818</u>

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
NOTES TO THE FINANCIAL STATEMENTS  
December 31, 1996 and 1995

**NOTE 7 - DEFEASED DEBT**

**Defeasance During 1995**

On August 31, 1995, the District issued \$85,800,000 1995 Series A Sewer System Improvement and Refunding Revenue bonds dated August 15, 1995, with an average interest rate of 5.75%. A portion of the proceeds from the bond issue was used to purchase U.S. Government Securities to advance refund \$5,795,000 of outstanding 1986 Series A bonds with an average interest rate of 7.2% and \$12,370,000 of outstanding 1991 Series A bonds with an average interest rate of 6.4%. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1986 Sewer A bonds maturing on and after December 1, 1997 assuming redemption on June 1, 1996 and the 1991 Series A bonds maturing on and after December 1, 2001 assuming redemption on June 1, 2001.

Although the advance refunding resulted in the recognition of an accounting loss of \$1,297,000 to be amortized over future periods in accordance with GASB 23, the District in effect reduced its aggregate debt service payments by \$967,000 and obtained an economic gain (difference between the present values of the old and new debt service payments) of \$779,000.

**Other Defeasance**

In prior years, MSD defeased various general obligation serial bonds and revenue serial bonds through refinancing and operations. Separate irrevocable trust funds were established and funded to fully service the defeased debt until the debt is called or matures. For financial reporting purposes, the debt has been considered defeased and is not included in the financial statements. At December 31, 1996 and 1995, the amount of prior year's defeased debt outstanding amounted to \$34,046,000 and \$107,000,000, respectively.

**NOTE 8 - CONTRIBUTIONS IN AID OF CONSTRUCTION**

Contributions have been received from the OWDA and the United States Government in accordance with agreements transacted between MSD and these two entities. The City of Cincinnati and Hamilton County provided working capital to MSD upon formation, and those capital contributions are included in the amounts below. Other contributions have been received in connection with the expansion of sewerage services.

**NOTE 8 - CONTRIBUTIONS IN AID OF CONSTRUCTION (Continued)**

As of December 31, 1996 and 1995, net contributions in aid of construction consisted of the following:

	(in thousands)	
	<u>1996</u>	<u>1995</u>
United States Government Grants	\$129,722	\$129,722
City of Cincinnati	68,356	68,300
Ohio Water Development Authority Grants	45,901	45,483
Customers	68,829	63,064
Hamilton County	<u>1,738</u>	<u>1,738</u>
	314,546	308,307
Less accumulated amortization of contributions in aid of construction	<u>(141,373)</u>	<u>(133,673)</u>
	<u>\$173,173</u>	<u>\$174,634</u>

**NOTE 9 - PENSION AND RETIREMENT**

All MSD full-time employees participate in either the Retirement System of the City of Cincinnati (City System) or the Public Employees' Retirement System administered by the State of Ohio (State PERS). Each plan is a cost-sharing, multiple-employer, public employee retirement system.

The payroll for employees covered by the plans for the year ended December 31, 1996, was \$26,808,000 and \$1,002,000 for the City System and State PERS, respectively. MSD's total payroll was \$27,810,000. The payroll for employees covered by the plans for the year ended December 31, 1995, was \$26,040,000 and \$1,037,000 for the City System and State PERS, respectively. MSD's total payroll for 1995 was \$27,077,000.

Income sources for each pension system include both employee and employer contributions as well as income earned on investments. Employer contributions to the pension funds are current and fully met as required by law. Annual contributions to all pension systems include a provision for past service costs to properly fund pension and other benefits payable on account for creditable service. Each pension system is evaluated annually by a nationally recognized actuarial consultant.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
NOTES TO THE FINANCIAL STATEMENTS  
December 31, 1996 and 1995

**NOTE 9 - PENSION AND RETIREMENT (Continued)**

The following table lists the employer and employee contribution rates and amounts paid by MSD for each retirement system for the year ended December 31, 1996.

	(in thousands, except percents)			
	<u>Employer</u>		<u>Employee</u>	
	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>
City of Cincinnati Retirement System	18.90%	\$5,223*	7.0%	\$1,877
Public Employees Retirement System	13.55%	\$ 136**	8.5%	\$ 85

\* Employer amount includes health care costs which were included in the calculation of the pension benefit obligation.

\*\* A portion of the PERS employer amount is used to fund a health care program which is not part of pension benefit obligation calculations.

The "pension benefit obligation" (PBO) is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits estimated to be payable in the future as a result of the employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess each system's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among retirement systems and employers. The measure is independent of the actuarial funding method used to determine contributions to the retirement system. The systems do not make separate measurements of assets and pension benefit obligation for individual employers.

Listed below is the pension benefit obligation for the City's system as a whole, net assets available for benefits, and the unfunded pension benefit obligation. These were determined through actuarial evaluation performed as of December 31, 1996.

	<u>Pension Benefit Obligation(PBO)</u>	(in thousands)	<u>Unfunded PBO</u>
		<u>Net Assets Available</u>	
City of Cincinnati Retirement System (City Employees only 88.452%)	\$ 1,170,068	\$ 1,331,324	\$ (161,256)

## NOTES TO THE FINANCIAL STATEMENTS

December 31, 1996 and 1995

## NOTE 9 - PENSION AND RETIREMENT (Continued)

## City of Cincinnati Retirement System

The service retirement allowance vests after five years of creditable service. Medical care benefits vest after fifteen years of creditable service or after reaching age sixty with five years of creditable service. Any member in service may retire upon attaining age sixty, regardless of length of membership service if he was enrolled prior to January 1, 1969, or with a least five years of membership service if enrollment occurred at January 1, 1969, or later; or upon completing five years of creditable service before age sixty members may retire with a retirement allowance commencing at age sixty, provided, however, at the time of election of the deferred annuity there is no loan outstanding against his contributions; or upon completing thirty or more years of membership service at any age, with a retirement allowance commencing immediately.

The annual retirement allowance consists of an annuity provided by the number equal in value to contributions with interest at the time of retirement and a pension, which together with annuity, produces a total annual retirement allowance equal to 2 percent of the average of the three highest years' compensation multiplied by the number of years of membership service. The System also provides death and disability benefits. These benefit provisions and all other requirements are established by the Cincinnati Municipal Code.

Each member contributes at a rate of seven percent (7%) of his salary until his retirement. The rate of contribution is fixed by the fund's Board of Trustees on the basis of authority provided by Chapter 203, Section 77, of the Cincinnati Municipal Code. MSD makes annual employer contributions based on a percentage of the salaries of all members. The contribution rate for 1996 was 18.90%.

The City System has 6,006 active contributing participants of which 702 are MSD employees. For 1996 MSD's contribution was 16 percent of the total employer contribution.

The following significant actuarial assumptions used for 1995 and 1996 to compute the pension benefit obligation are the same as those used to compute actuarial determined contribution requirements.

- |                       |  |
|-----------------------|--|
| 1. Investment Return: | 8.75% prior to the deduction of expenses per annum, compounded annually and adding an expense assumption to the determination of the plan's normal cost. |
| 2. Mortality:         | a) Non-disabled - 1983 Group Annuity Mortality Table.<br>b) Disabled - Pension Benefit Guarantee Corp. Disabled Mortality Table.                         |

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
NOTES TO THE FINANCIAL STATEMENTS  
December 31, 1996 and 1995**

**NOTE 9 - PENSION AND RETIREMENT (Continued)**

- |                            |   |
|----------------------------|---|
| 3. Salary Scale:           | 4.25% per annum for projected salary in 1996 and 4.5% thereafter with select rates during the first three years of service plus provision for an additional 9% increase in final average salary due to final lump sum salary payment.   |
| 4. Rate of Termination:    | 1995 City of Cincinnati Experience Table.   |
| 5. Rate of Disability:     | 1995 City of Cincinnati Experience Table.   |
| 6. Asset Valuation:        | Preliminary actuarial value of assets is calculated by projecting the prior year's actuarial value to the current valuation date using the valuation interest assumption and actual contributions, benefit payments and expenses. This preliminary value is then adjusted if it is not within a corridor equal to 90%-110% of the market value of assets. |
| 7. Assumed Retirement Age: | Table of rates from age 47 to 70.   |
| 8. Medical Benefits:       | Current premium costs with projected increases of 7% per annum for post retirement benefit increases.   |

The "entry age normal with frozen initial liability" is the funding method used by the actuary in computing the employer contribution rate and estimated actuarial liability of the system. The unfunded actuarial liability at December 31, 1996, was \$66,176,271.

Trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due. Ten-year trend information is available and the Analysis of Funding Progress is available for years 1987 through 1996.

**Other Postemployment Benefit Information**

The City System provides hospital and surgical insurance to retired members who have earned fifteen years credited service at the time of termination or terminate after age sixty with five years credited service. Those who are receiving survivor benefits of eligible members are entitled to have their hospital and surgical insurance premiums paid by the System. When benefits would be reduced by reason of the retired member's eligibility for hospital and medical benefits under federal social security laws, the System will pay whatever additional fees are required for the federal medical coverage.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI  
NOTES TO THE FINANCIAL STATEMENTS  
December 31, 1996 and 1995

**NOTE 9 - PENSION AND RETIREMENT (Continued)**

The health care coverage provided by the City System is considered an Other Postemployment Benefit (OPEB). It is advance funded on an actuarial determined basis as a portion of the employer contribution requirement to the System. The Cincinnati Municipal Code provides authority for employer contributions. Health care coverage has been included in the calculation of the pension benefit obligation. Assets and liabilities are not separately determined.

**Public Employees' Retirement System**

MSD has 25 employees, as of December 31, 1996, who are participants of the Public Employees' Retirement System administered by the State of Ohio. This plan is not a significant portion of the overall operations of MSD. Additional disclosures concerning this plan, including other postemployment benefit information, can be found in the plan's annual financial statements.

**NOTE 10 - RELATED PARTY TRANSACTIONS**

Cincinnati Water Works provides billing and collection services on customers' accounts for MSD. Fees for these services for 1996 and 1995 were \$3,057,000 and \$2,978,000, respectively. Fees are also paid to other municipalities and villages within Hamilton County for collection of sewerage bills.

The City of Cincinnati provides "overhead" services to MSD, such as check disbursement, investment and legal services, etc. The fees for these services for 1996 and 1995 were \$2,177,000 and \$1,950,000, respectively. In addition, the City's Municipal Garage provides gasoline and repairs vehicles for MSD. Fees for these services were \$935,000 and \$901,000 for 1996 and 1995, respectively.

**NOTE 11 - COMMITMENTS AND CONTINGENCIES**

The City of Cincinnati and the Board of County Commissioners of Hamilton County, Ohio, are parties to a Federal Consent Order which was entered in settlement of United States of America vs. The Board of County Commissioners of Hamilton County, Ohio, et al. Case No. C-1-85-0693. The City and County have continued in their efforts to negotiate an amendment to change certain construction schedules appearing in exhibits to that order. The City and County believe these changes are due to circumstances beyond the control of either, and are seeking approval of those schedule modifications from the United States Environmental Protection Agency. The consent order provides for stipulated penalties for failure to meet certain construction schedule deadlines but specifically contemplates that no such penalties will be collected from either defendant where the non-compliance was beyond the reasonable control of the defendants. In addition, according to MSD's Chief Legal Counsel, EPA has requested the payment of \$290,000 in stipulated penalties under the Consent Order for certain effluent limit excursions. The Consent order provides for stipulated penalties under certain conditions, and although the City and County have argued that no substantial penalties are appropriate, it appears that EPA does intend to extract some monetary payment for the excursions. Currently, the City is awaiting EPA's response to certain defenses presented during 1992.

**NOTE 11 - COMMITMENTS AND CONTINGENCIES (Continued)**

As part of the District's capital improvement program the District has entered into a number of contracts for construction, design, and other services. Commitments under these contracts aggregate approximately \$36 million as of December 31, 1996.



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**INDEPENDENT AUDITORS' REPORT ON THE  
INTERNAL CONTROL STRUCTURE**

The Honorable Board of County Commissioners  
The Metropolitan Sewer District of Greater Cincinnati  
County of Hamilton, Ohio

We have audited the financial statements of The Metropolitan Sewer District of Greater Cincinnati (MSD) as of and for the year ended December 31, 1996 and have issued our report thereon dated April 25, 1997.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of MSD is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the December 31, 1996 financial statements of MSD, for the year ended December 31, 1996, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

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Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that errors and irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above.

This report is intended for the information of the Hamilton County Board of Commissioners, the Auditor of the State of Ohio, and the cognizant federal audit agency. However, this report is a matter of public record and its distribution is not limited.

*VonLehman & Company Inc.*

Fort Mitchell, Kentucky  
April 25, 1997



VONLEHMAN & COMPANY INC.

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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE  
WITH LAWS AND REGULATIONS RELATING TO THE  
FINANCIAL STATEMENTS**

The Honorable Board of County Commissioners  
The Metropolitan Sewer District of Greater Cincinnati  
County of Hamilton, Ohio

We have audited the financial statements of the Metropolitan Sewer District of Greater Cincinnati, Cincinnati, Ohio, as of and for the year ended December 31, 1996, and have issued our report thereon dated April 25, 1997.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States and the provisions of Office of Management and Budget Circular A-128, "Audits of State and Local Governments." Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

We have also applied procedures to test MSD's compliance with provisions of laws and regulations that the Auditor of State has determined to be significant as a matter of public policy, public stewardship, or public accountability, as identified in the Auditor of State's Ohio Compliance Supplement, revised December, 1989, for the year ended June 30, 1996.

Compliance with laws, regulations, contracts, and grants applicable to MSD is the responsibility of MSD's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatements, we performed tests of MSD's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

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This report is intended for the information of the Hamilton County Board of Commissioners, the Auditor of the State of Ohio, and the cognizant federal audit agency. However, this report is a matter of public record and its distribution is not limited.

*VonLehman & Company Inc.*

Fort Mitchell, Kentucky  
April 25, 1997